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BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 88-608-W - ORDER NO. 90-152 ✓
FEBRUARY 13, 1990

IN RE: Application of Harbor Island Utilities,)
Inc., for approval of new schedules of) ORDER
rates and charges for water service) APPROVING
provided to its customers in its service) RATES AND
area on Harbor Island, Beaufort County,) CHARGES
South Carolina.)

I.

INTRODUCTION

This matter comes before the Public Service Commission of South Carolina (the Commission) by way of an Application filed with the Commission on August 17, 1989, by Harbor Island Utilities, Inc. (the Company or Harbor Island) whereby the Company seeks approval of new schedules of rates and charges for water service provided to its customers in its certified service area on Harbor Island, Beaufort County, South Carolina. The Application was filed pursuant to S.C. Code Section 58-5-240 (1976), as amended, and R.103-821 of the Commission's Rules of Practice and Procedure.

By letter dated August 25, 1989, the Commission's Executive Director instructed the Company to cause to be published a prepared Notice of Filing, one time, in a newspaper of general circulation in the area affected by the Company's Application. The Notice of Filing was likewise published in the State Register, Vol. 13, Issue

No. 9, dated September 20, 1989. The Notice of Filing indicated the nature of the Company's application and advised all interested parties desiring participation in the scheduled proceeding of the manner and time in which to file the appropriate pleadings. The Company was likewise required to notify directly all customers affected by the proposed rates and charges.

A Petition to Intervene was filed by Henry H. Schulte, Jr., a resident of Harbor Island. Several letters of Protest were filed opposing the requested increase.

The Commission Staff made on-site investigations of the Company's facilities, audited the Company's books and records, and gathered other detailed information concerning the Company's operations.

A public hearing relative to the matters asserted in the Company's application was commenced in the Offices of the Commission on January 9, 1990 at 11:00 a.m. in the Commission's Hearing Room. Pursuant to Section 58-3-95, S.C. Code of Laws (Cum. Supp. 1989), a panel of three members composed of Commissioner Yonce presiding, and Commissioners Butler and Fraizer, was designated to hear and rule on this matter. Scott A. Elliott, Esquire, represented the Company; and Marsha A. Ward, General Counsel, represented the Commission Staff.

The Company presented the testimony of R. Arnold Ellison, President of Community Services Management, Inc. which provides professional services in management operation and consulting services for the Company and is the parent company of Harbor

Island, to explain the services being provided by the Company, the financial statements and accounting adjustments submitted, and the reasons for the requested rate increase. The Commission Staff presented Joe Maready, Public Utilities Accountant, and Fred E. Brock, Public Utilities Rate Analyst, to report Staff's findings and recommendations. Mr. Schulte did not prefile his intended testimony in this matter but he did appear to testify at the hearing. His appearance was given the status of a Protestant.

II

JURISDICTION

S.C. Code Ann., Section 58-5-290 (1976) vests this Commission with the authority to change the rates of a "public utility" whenever the Commission finds, after hearing, that such rates are "unjust, unreasonable, noncompensatory, inadequate, discriminatory or in any wise in violation of any provision of law." A public utility is defined by S.C. Code Ann., Section 58-5-10(3) (1976) as including "every corporation and person furnishing or supplying in any manner, gas, heat (other than by means of electricity), water, sewerage collection, sewerage disposal and street railway service, or any of them, to the public, or any portion thereof, for compensation." Section 58-5-290 also provides that when the Commission determines that a utility's rates are unlawful, the Commission shall determine and fix by order the "just and reasonable" rates to be thereafter charged by the public utility. The Commission finds and concludes in this proceeding that the Company is a public utility under the provisions of S.C. Code Ann.,

Section 58-5-10(3) (1976).

III.

RATEMAKING METHODOLOGY

Under the guidelines established in the decisions of Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia, 262 U.S. 679 (1923), and Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944), this Commission does not ensure through regulation that a utility will produce net revenues. As the United States Supreme Court noted in the Hope Natural Gas decision, supra, the utility "has no constitutional rights to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures." However, employing fair and enlightened judgment and giving consideration to all relevant facts, the Commission should establish rates which will produce revenues "sufficient to assure confidence in the financial soundness of the utility and...that are adequate under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties." Bluefield, supra, at 692-693.

Neither S.C. Code Ann., Section 58-5-290 (1976), nor any other statute prescribes a particular method to be utilized by the Commission to determine the lawfulness of the rates of a public utility. For ratemaking purposes, this Commission examines the relationships between expenses, revenues and investment in a historic test period because such examination provides a constant and reliable factor upon which calculation can be made to formulate

the basis for determining just and reasonable rates. This method was recognized and approved by the Supreme Court for ratemaking purposes involving utilities in Southern Bell Telephone and Telegraph Co. v. The Public Service Commission of S.C., 270 S.C. 590, 244 S.E. 2d 278 (1978).

The historic test period generally utilized is the most recent twelve-month period for which reasonably complete financial data is available, and is referred to as the "test year" period. In this proceeding, the Commission concludes that the twelve-month period ending October 31, 1988, should be used as the test year. This Commission allows certain accounting and pro forma adjustments to be made to the actual test year figures. Adjustments are made for (1) items occurring in the test year but which are not subject to recur in the future; (2) items of an extraordinary nature whose effects must be annualized or normalized to reflect properly their impact; and (3) other items which should be included or excluded for ratemaking purposes. Adjustments are also made for "known and measurable changes" in expenses, revenues and investments occurring after the test year. Southern Bell Telephone & Telegraph Co., v. Public Service Commission, 270 S.C. 590, 244 S.E. 2d 278 (1978).

For water utilities, where the utility's rate base has been substantially reduced by customer donations, tap fees, contributions in aid of construction and book value in excess of investment the utility may request, or the Commission may decide, to use the "operating ratio" and/or "operating margin" as guides in determining just and reasonable rates, instead of examining the

utility's return on its rate base. The operating ratio is the percentage obtained by dividing total operating expenses by operating revenues. The obverse side of this calculation, the operating margin, is determined by dividing net operating income for return by the total operating revenues of the utility.

In this proceeding, the Commission will use the operating margin as a guide in determining the lawfulness of the Company's proposed rates and if necessary, the fixing of just and reasonable rates. This method was recognized as an acceptable guide for ratemaking purposes in Patton v. South Carolina Public Service Commission, 280 S.C. 288, 312 SE 2d 257 (1984).

IV.

ACCOUNTING AND PRO FORMA ADJUSTMENTS

The Company and the Staff proposed adjustments to revenues and expenses in their presentations. Company witness Ellison accepted the adjustments made by the Staff for the purposes of this proceeding and for ratemaking purposes with three exceptions. Namely, the Company and the Staff differed over the appropriate amounts to be included in the Company's expenses for engineering reports and studies for rate case expenses, legal fees for rate case expenses, and expenses for painting the water tank.

Staff's audit revealed that Community Services Management (CSM) had billed Harbor Island \$5,000 for a rate study. Staff proposed to amortize that amount over three years. The Company had proposed total rate case engineering expenses of \$6,000 to be amortized over three years, which represented an additional \$1,000,

fee of CSM for appearing at the Commission hearing and hearing preparation which had not been billed. At the hearing, Mr. Ellison presented an invoice which had been presented to Harbor Island by CSM for the additional \$1,000 rate case expenses. The Commission has determined that the additional \$1,000, having been presented to the Company for payment, is a known and measurable expense. The Commission accepts the Company's adjustment on this issue now that the proper documentation has been provided.

A similar difference existed concerning the Company's legal expenses. At the time of the Staff Audit, no legal fees had been submitted to the Company for rate case expenses. The Company estimated legal fees of \$3,000, amortized over three years. At the hearing, Mr. Ellison presented a bill for legal fees in the amount of \$2,968.50. The Commission accepts the amount submitted at the hearing as being known and measurable and will amortize such expenses over three years.

The Company proposes to increase its expenses for painting its ground storage tank. According to witness Ellison, the tank is in immediate need of painting, but the utility does not have adequate funds to enter into a contract to have both the outside and the inside of the tank painted. The Company has received a proposal from a contractor to perform the work. The proposal was submitted into evidence as Hearing Exhibit No. 2. The proposal states a sum of \$6,680 to paint the exterior of the tank and \$18,409 to paint the interior of the tank. Mr. Ellison testified that the Company intends to paint the exterior as soon as possible, assuming the

expense is allowed, and to paint the interior after one year. The Company proposes to amortize the exterior painting expenses over a five year period and to amortize the interior painting expenses over ten years.

The Commission Staff did not propose such an adjustment. The Commission does not allow expenses that are not known and measurable. In this case, while the Company asserts that the ground storage tank needs painting and it intends to do so as soon as the rates are approved, the Company has not commenced the painting nor has it executed the proposal submitted by the contractor. The proposal provides that it may be withdrawn if not accepted within 120 days. Therefore, if Harbor Island does not accept the proposal within the allowed time and the proposal is withdrawn, a new proposal may provide for different amounts to perform the work. Unless the contract is accepted by the Company and the amount required to perform the work is set or unless the work has commenced, it is not a known and measurable expense and is not allowed for ratemaking purposes. The Commission finds, for the above reasons, that the expenses for painting the ground storage tank are not know and measurable, should not be allowed for ratemaking purposes, and the Company's adjustment is not accepted by the Commission.

The other adjustments proposed by Staff and supported by the Staff Report (See, Hearing Exhibit No. 3) are in accord with the Commission's accepted ratemaking and regulatory policies as well as generally accepted accounting principles and generally accepted

accounting standards. Based upon the stipulation of the Company and the accepted accounting principles and practices employed by the Commission Staff in its audit of the Company's books and records, the Commission finds and concludes that all other Staff adjustments to revenues and expenses in this proceeding are proper and necessary, and are adopted for the reasons detailed by the Staff in its Report and in its testimony.

V.

DISCUSSION

The following Table indicates the Company's gross revenues for the test year, after accounting and pro forma adjustments under the presently approved schedules; the Company's operating expenses for the test year after accounting and pro forma adjustments; and the operating margin under the presently approved schedules for the test year:

Table A

Operating Revenues	\$ 70,189
Operating Expenses	78,260
Total Operating Income (Loss)	\$ (8,071)
Add: Customer Growth	(32)
Operating Income (Loss)	\$ <u>(8,103)</u>
Operating Margin	<u>(11.54)%</u>

The following Table shows the effect of the Company's proposed rate schedule, after accounting and pro forma adjustments approved herein:

Table B

Operating Revenues	\$ 106,474
Operating Expenses	83,940
Total Operating Income	\$ 22,534
Add: Customer Growth	90
Operating Income (Loss)	\$ 22,624
Operating Margin	<u>21.25%</u>

The Commission is mindful of those standards delineated in the Bluefield decision, supra, and of Patton, supra. The Commission must achieve a balance between the respective interests of the Company and of the consumer. The Commission has considered the spectrum of relevant factors in this proceeding, including the adopted accounting adjustments to expenses, the revenue requirements for the Company, the proposed average price of \$25.23 per month for residential customers for which the Company's service is rendered, the quality of that service which was not complained of by any customer, and the effect of the proposal upon the customer, which amounts to a 57.66% increase to the residential customer, over 100% increase to the commercial customer and significant increases to the multi-unit and irrigation customers.

The three fundamental criteria of a sound rate structure have been characterized as follows:

...(a) the revenue-requirement or financial-need objective, which takes the form of a fair-return standard with respect to private utility companies; (b) the fair-cost apportionment objective which invokes the principle that the burden of meeting total requirements must be distributed fairly among the beneficiaries of the service; and (c) the optimum-use or consumer rationing under which the rates are designed to discourage the wasteful use of public utility services while promoting all use that is

economically justified in view of the relationships between costs incurred and benefits received.

Bonbright, Principles of Public Utility Rates
(1961), p.292.

The magnitude of the proposed increase from \$16.00 per month to an average of \$25.23 per month for residential customers, as well as the percentage increase to the other classes of customers causes the Commission to closely examine the requested monthly rates to determine whether the Company has adequately justified such. With the perspective afforded by the revenue results of the proposed increase in rates and the resultant operating margin of 21.25%, depicted in Table B, supra, the Commission has determined that the proposed schedule of rates designed to produce those revenues are unjust and unreasonable as producing excessive revenues.

Upon this finding it is incumbent upon the Commission to approve rates which are just and reasonable, not only producing revenues and an operating margin within a reasonable range, but which also distribute fairly the revenue requirements, considering the price for which the Company's service is rendered and the quality of that service. In light of those factors and based upon the record in the instant proceeding, the Commission concludes that the Company's level of operating revenues should be \$100,838 which results in a fair operating margin that the Company should have an opportunity to earn of 17.94%. The following table reflects an operating margin of 17.94%:

TABLE C

Operating Revenues	\$ 100,838
Operating Expenses	82,816
Total Operating Income	\$ 18,022
Add: Customer Growth	72
Operating Income	\$ 18,094
Operating Margin	<u>17.94%</u>

The Commission has certain discretionary authority when it comes to supervising and regulating the rates and service of public utilities in this state pursuant to S.C. Code Ann. Section 58-5-210 (1976). The determination of an appropriate operating margin is such an area where the Commission may exercise its discretion. See, Patton, supra. It is the Commission's duty, in determining the just and reasonable operating margin for Harbor Island, to examine the relationship between the Company's expenses, revenues and investment in an historic test period, as well as the quality of service provided to its customers and the impact of the proposed rates on the customers.

Witness Schulte demonstrated the effect of the proposed increase on his personal residential bill as well as a rental unit he owns in Cedar Reef Villas. Based upon the impact on his monthly bill, the impact on his rental unit and the Homeowners Association's irrigation rate, he requested the Commission to reduce the Company's request. Mr. Schulte also pointed out that if Harbor Island's rates are substantially higher than neighboring Fripp Island, development will not take place as rapidly on Harbor

Island.

The required annual operating revenues of \$100,838 are obtained by reducing the proposed monthly residential water user fee rate by \$2.00 for each size meter. This reflects the Commission's determination that this level of revenues is appropriate, using the operating margin as a guide. The proposed commodity charge of \$2.50/1,000 gallons is approved. The Commission denies the requested Disconnect/Reconnect fee of \$75.00 due to nonpayment. The Company did not demonstrate that a greater fee was justified for nonpayment than the \$50 fee to reconnect/disconnect at the customer's request. Therefore, the appropriate reconnect/disconnect fee, by way of a customer request or for nonpayment will be \$50.00. Mr. Ellison explained during the hearing that the Company buys its water from the Beaufort/Jasper Water and Sewer Authority and that Beaufort/Jasper may increase its rates at any time. Additionally, the Company depends on Fripp Island Public Service District to transport the purchased water from St. Helena to Harbor Island for a fee. This transportation fee may be increased by Fripp Island. Because of the potential for these fees to be increased without notice to Harbor Island, the Company requests that it be allowed to automatically increase its base rate and water overage rate by 115% of the any Beaufort/Jasper wholesale rate increase and/or any Fripp Island transportation rate increase as they might occur. The Commission views the amounts paid for purchased water and transportation fees to be similar to any other expense incurred by the Company in providing water

service to its customers. This would include electric expenses, telephone expenses, etc. Just because an increase in an operating expense occurs, it does not warrant an automatic increase in rates. Witness Ellison admitted that there was a profit margin reflected in his retail rate to the Harbor Island customers compared to the wholesale rate paid to Beaufort/Jasper and Fripp Island. The Commission can not allow rates to be increased without a hearing pursuant to S.C. Code Ann., §58-5-240 (Cum. Supp. 1989).

Therefore, the Company's proposal is denied. The Commission denies the Company's proposed returned check charge of \$15.00. It is the Commission's opinion that S.C. Code Ann., §34-11-70 (Cum. Supp. 1989) provides the proper remedy to the Company, and the Commission does not have jurisdiction to approve such a charge.

The Commission has developed a schedule of rates and charges, attached hereto as Appendix A and incorporated by reference herein, to apply to the water service provided by the Company.

The Commission finds and concludes that the rates and charges approved herein achieve a balance between the interest of the Company and those of its affected customers. This results in a reasonable attainment of our ratemaking objectives in light of applicable statutory safeguards.

IT IS THEREFORE ORDERED:

1. That the proposed schedule of rates and charges by the Company are hereby found to be unreasonable and are denied.

2. That the schedules of rates and charges attached hereto as Appendix A, be, and hereby are, approved for service rendered

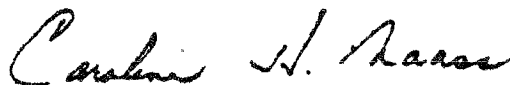
on or after the date of this Order, and that these schedules be, and are hereby, deemed to be filed with the Commission pursuant to S.C. Code Ann. Section 58-5-240 (1976).

3. That should such schedule not be placed in effect within three (3) months of the effective date of this Order, such schedule as contained herein shall not be charged without written permission from the Commission.

4. That the Company shall maintain its books and records for its water operations in accordance with the NARUC Uniform System of Accounts for Class C Water Utilities, as adopted by this Commission.

5. That this Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:



Chairman

ATTEST:


Executive Director

(SEAL)

DOCKET NO. 88-608-W - ORDER NO. 90-152
HARBOR ISLAND UTILITIES, INC.
FEBRUARY 12, 1990
APPENDIX A

The Rate Schedule Is As Follows:

USER FEES - WATER

1. Residential

3/4" meter	0 - 2,000 gals	\$20.00/month
	Over 2,000 gals	\$ 2.50/1,000 gals
1" meter	0 - 2,000 gals	\$23.00/month
	Over 2,000 gals	\$ 2.50/1,000 gals
1-1/2" meter	0 - 2,000 gals	\$33.00/month
	Over 2,000 gals	\$ 2.50/1,000 gals

2. Commercial Water Service

3/4" meter	0 - 2,000 gals	\$30.00/month
	Over 2,000 gals	\$ 2.50/1,000 gals
1" meter	0 - 2,000 gals	\$35.00/month
	Over 2,000 gals	\$ 2.50/1,000 gals
1-1/2" meter	0 - 2,000 gals	\$50.00/month
	Over 2,000 gals	\$ 2.50/1,000 gals

3. Landscape Irrigation

3/4" meter	0 - 2,000 gals	\$20.00/month
	Over 2,000 gals	\$ 2.50/1,000 gals
1" meter	0 - 2,000 gals	\$23.00/month
	Over 2,000 gals	\$ 2.50/1,000 gals
1-1/2" meter	0 - 2,000 gals	\$33.00/month
	Over 2,000 gals	\$ 2.50/month

4. Meters used for Multiple Residential Units

Minimum monthly charge @ \$20.00/unit provides
0 - 2,000 gallons/unit
Excess over 2,000 gals. x no. of units \$2.50/1,000 gals

NOTE: All rates above are for monthly service. The Utility will bill on a quarterly basis at 3 times the base rate plus any water used in excess of 6,000 at \$2.50/1,000 gallons.

FIRE HYDRANT USAGE

1. Installation Charge	\$50.00
Advance Payment	\$50.00
Cost per 1,000 gallons	\$ 2.50

RECONNECTION FEES

1. Disconnect/Reconnect at Customer's Request	\$50.00
2. Disconnect/Reconnect due to Nonpayment	\$50.00

TAP FEES*

1. Single Units

3/4" meter	\$ 500.00*
1" meter	\$ 850.00*
1-1/2" meter	\$1000.00
2" meter	\$2000.00

2. Master Meter for Multiple Units

1" - 2"	\$500.00 per unit served
Greater than 2"	\$350.00 per unit plus cost of meter installation

ADVANCE PAYMENT

1. For Water Used During Construction (paid with Tap Fees)	\$100.00
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*No changes to presently approved rates.